

Message Text

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ACTION NEA-10

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FM AMEMBASSY ISLAMABAD
TO SECSTATE WASHDC IMMEDIATE 6804

C O N F I D E N T I A L SECTION 1 OF 3 ISLAMABAD 3893

PASS USDA

E.O. 11652: GDS
TAGS: EFIN, EAID, PK, AGR
SUBJECT: GOP WHEAT PROCUREMENT ARRANGEMENT, AND PL-480 STRATEGY

SUMMARY: JUST BEFORE MAIN WHEAT HARVEST GOP HAS ADOPTED A SET OF MEASURES RE PROCUREMENT OF WHEAT WHICH REVERSE MUCH OF STRATEGY ADOPTED SINCE 1974 FOR INCREASING WHEAT PRODUCTION AND THREATEN GAINS OF RECENT YEARS. PRESSED BY NEED TO MAINTAIN GOVERNMENT STOCKS FOR RATION SHOP ISSUANCES AND AVERT POSSIBLE URBAN UNREST, GOVERNMENT HAS IMPOSED RESTRICTIONS ON MOVEMENT AND STORAGE IN ORDER TO ASSUME A NEAR MONOPSONY POSITION AT HARVEST. HOWEVER, THIS WILL PUSH DOWN FARMGATE PRICE, FAIL TO PROVIDE APPROPRIATE PRODUCTION INCENTIVE, AND IS IN FACT A LEVY ON FARMERS TO MAINTAIN LOW FOOD PRICES IN POLITICALLY VOLATILE CITIES. REAL DILEMMA IS FACED BY GOP. HOWEVER, THIS PROVIDES A CLEAR OPPORTUNITY TO START TO DEVELOP A MULTI-YEAR PROGRAM LINKING LEVEL OF PL-480 ASSISTANCE TO REALISTIC AGRICULTURAL DEVELOPMENT POLICIES. DESIREABLE ELEMENTS OF SUCH A PROGRAM INCLUDE: (A) A BETTER GOP SUPPORT PRICE PROGRAM RESPONSIVE TO COST OF INPUTS; (B) ELIMINATION OF MARKETING RESTRICTIONS AND USE OF OPEN MARKET SALES FROM RESERVES; (C) A GRAIN RESERVE OF ABOUT ONE MILLION TONS; (D) REFORM OF THE RATION SYSTEM TO FOCUS IT
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UPON THE POOR AND REDUCE EXCESSIVE ISSUANCES. CHANCES FOR SUCCESS ARE IMPROVED IF THE PROGRAM IS DEVELOPED COLLEGIALLY WITH THE GOP SO THAT IT ONLY AGREES TO WHAT IT FINDS REALISTIC BUT IS THEN HELD TO THE AGREED MULTI-YEAR PROGRAM. WE THINK THAT FOR THE GOP TO TAKE DIFFICULT STEPS NEEDED TO GET AGRICULTURAL DEVELOPMENT MOVING AGAIN WILL REQUIRE THE PROSPECT OF SUBSTANTIALLY INCREASED PL 480 ASSISTANCE AS A CUSHION. WE

TENTATIVELY HAVE IN MIND A PROGRAM LEVEL PROVIDING AN ADDITIONAL 150,000 MT OF WHEAT IN FY 78 AND 550,000 MT IN FY 79 WITH FUTURE YEAR COMMITMENTS DEPENDENT ON THE PROGRAM DEVELOPED AND PAKISTANI PERFORMANCE UNDER IT.

ACTION REQUESTED: PROMPT WASHINGTON AGENCY REVIEW OF THIS PROPOSAL AND CONSIDERATION OF THE TENTATIVE PROGRAM LEVELS PROPOSED ABOVE. END SUMMARY

1. FOR SOME YEARS WE HAVE BEEN TRYING TO USE PL 480 WHEAT AID TOGETHER WITH FERTILIZER IMPORTS AS THE MOST IMPORTANT TOOLS IN HELPING THE GOP IMPLEMENT A STRATEGY INTENDED TO INCREASE WHEAT PRODUCTITC AND ASSURING SUPPLIES AT A LEVEL THAT WOULD PREVENT SHARP PRICE INCREASES. THE STRATEGY HAS BEEN LARGELY SPELLED OUT IN THREE DOCUMENTS. THE FIRST IS THE SEPTEMBER 9, 1975 PROJECT PAPER (AID-DLC/P-2129) FOR THE FERTILIZER LOAN (391-4041). THIS SPELLS OUT POLICY INITIATIVES BY THE GOP (GOP INPUTS), AND HOW THESE CONTRIBUTE TO THE ENDS SOUGHT. (SEE PARTICULARLY GOP LETTER OF APPLICATION AND LOGICAL FRAMEWORK.) THE SECOND WAS THE FIVE YEAR TITLE I STRATEGY SENT TO WASHINGTON AS A USAID AUGUST 1976 SUBMISSION. THE LAST IS THE NEGOTIATING MINUTES OF THE DECEMBER 22, 1977 PL 480 AGREEMENT.

2. PAKISTAN HAS, LIKE MOST OF SOUTH ASIA, AN ESTABLISHED SYSTEM OF GOVERNMENT CONTROLLED RETAIL OUTLETS FOR SELLING BASIC FOODSTUFFS AT A CONTROLLED, USUALLY SUBSIDIZED PRICE. IN PAKISTAN THE MAJOR ITEM DISTRIBUTED IS WHEAT FLOUR. KEEPING THE RATION CONFIDENTIAL

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SHOPS ADEQUATELY SUPPLIED HAS BEEN THE MAJOR PREOCCUPATION OF THE FEDERAL AND PROVINCIAL FOOD AGENCIES, WHO DEPEND UPON PROCUREMENT OF DOMESTIC WHEAT AT HARVEST TIME AND IMPORTS THROUGHOUT THE YEAR. THE WHEAT PRODUCTION STRATEGY THE GOP ADOPTED IN 1974 HAS BEEN TO USE THE HARVEST PROCUREMENT SYSTEM TO PLACE A FLOOR UNDER THE HARVEST PRICE OF WHEAT, AND ALLOW UNRESTRICTED INTERNAL TRADE IN WHEAT SO THAT THE NORMALLY HIGHER PRICES OF WHEAT AND FLOUR IN THE WHEAT DEFICIT (MOSTLY URBAN) AREAS ARE PASSED ON TO FARMERS. THIS FREE TRADE ALSO ACTS TO BRING DOWN THE PRICE IN THE DEFICIT AREAS WHEN SUPPLIES ARE ADEQUATE. FREE MARKET PRICE IN THE CITIES IS NORMALLY HIGHER THAN THE RATION SHOP PRICE, PARTLY BECAUSE MORE AFFLUENT CONSUMERS SEE RATION SHOP FLOUR AS AN INFERIOR PRODUCT WHICH MOST WILL BUY ONLY WHEN THE DIFFERENTIAL IS TOO GREAT.

3. PL 480, FAC, AND OTHER WHEAT IMPORTS HAVE HELPED THE GOVERNMENT KEEP THE PRICE DIFFERENTIAL UNDER CONTROL. THE KEY HAS BEEN TO MAINTAIN A RELATION BETWEEN THE FARM PRICE OF WHEAT AND THE COST OF WATER, FERTILIZER AND OTHER INPUTS THAT PROVIDES A CONTINUED INCENTIVE TO ADDITIONAL INVESTMENTS BY FARMERS IN FERTILIZER, HYV SEEDS, AND BETTER PRACTICES TO BOOST OUTPUT. WE BELIEVE THIS STRATEGY HAS BEEN A

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MAJOR FACTOR IN THE INCREASES IN WHEAT OUTPUT
ACHIEVED IN LAST FOUR YEARS.

4. LAST YEAR THIS STRATEGY BEGAN TO UNRAVEL WHEN FERTILIZER
SUPPLIES FELL SHORT OF FARMER DEMAND. DELAY IN U.S.
FINANCING (STILL IN ABEYANCE) OF DAP IMPORTS WAS ONE
FACTOR AND GOP RELUCTANCE TO USE ITS OWN SCARCE FOREIGN
EXCHANGE TO MEET NEEDS WAS ANOTHER. PURELY ACCIDENTAL
PROCUREMENT PROBLEMS WITH ALREADY PLANNED AND BUDGETED
IMPORTS AND WITH CANADIAN FERTILIZER ALSO CONTRIBUTED TO
SUPPLY SHORTAGE.

5. NOW AS 1977-78 HARVEST APPROACHES GOP HAS ADOPTED
A SET OF MEASURES RE PROCUREMENT OF WHEAT CROP WHICH
WE VIEW AS CONSTITUTING MAJOR PRODUCTION DISINCENTIVES.
UPWARD ADJUSTMENT IN PURCHASE PRICE OF RS. 37 PER
MAUND WHICH HAS BEEN IN EFFECT FOR THREE YEARS OF RISING
GENERAL PRICE LEVEL WAS CONSIDERED BY COUNCIL OF ADVISERS
BUT REJECTED. SIND AND PUNJAB PROVINCIAL GOVERNMENTS
HAVE BANNED INTER-DISTRICT MOVEMENT OF WHEAT AND PLACED
LIMITS ON AMOUNTS WHICH CAN LEGALLY BE STORED. MARKET
PRICES FOR WHEAT WERE RECENTLY RS. 60 PERMAUND, AND ARE
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DECLINING WITH ONSET OF HARVEST THEY ARE NOT EXPECTED TO FALL TO LEVEL OF OFFICIAL PURCHASE PRICE. MOST OBSERVERS CONTINUE TO PREDICT A TOTAL HARVEST AT LEAST marginally DOWN FROM LAST YEAR AS RESULT OF PROBLEMS WITH AVAILABILITY OF SEED AND FERTILIZER, AND VARIOUS DISEASE AND WEATHER CONSIDERATIONS. THIS WILL NECESSITATE INCREASED IMPORTS DURING THE COMING YEAR. WE WILL PROVIDE AN UPDATE ON CURRENT PRODUCTION ESTIMATES O/A MAY 15.

6. GOP IS NOW FACED WITH A VERY AWKWARD DILEMMA. THEY SEE ANY INCREASE IN THE PURCHASE PRICE OF WHEAT AS REQUIRING EITHER AN EQUIVALENT INCREASE IN PRICE OF RATION SHOP ATTA (FLOUR) IN ORDER TO KEEP WITHIN BUDGETARY PROVISION FOR SUBSIDY, OR ABANDONMENT OF THE TIGHT ANTI-INFLATIONARY BUDGET. HOWEVER, THEY ALSO BELIEVE INCREASE IN PRICE OF ATTA, THE SINGLE MOST IMPORTANT CONSUMER ITEM, IS UNTHINKABLE AT TIME WHEN MARTIAL LAW AUTHORITIES ALREADY FACE A SERIOUS TEST OF ITS ABILITY TO MAINTAIN LAW AND ORDER AS BHUTTO CASE UNFOLD. GOVERNMENT STOCKS FROM DOMESTIC PROCUREMENT OF ABOUT 2 MILLION TONS PLUS 1 MILLION OF IMPORTS WILL BE NEEDED TO MAINTAIN SUPPLIES FOR RATION SHOPS, MILITARY AND OTHER INSTITUTIONS. GOP FEARS THAT IF THEY ALLOW UNRESTRICTED MOVEMENT AND PRIVATE STORAGE OF WHEAT, FOOD DEPARTMENT CANNOT COMPETE WITH FREE MARKET AND MEET PROCUREMENT TARGETS AT PRICE OF RS. 37 PER MAUND. THEREFORE THEY IMPOSED RESTRICTIONS ON MOVEMENT AND STORAGE.

7. THIS POLICY AND PRICE NOT ONLY FAIL TO PROVIDE APPROPRIATE PRODUCTION INCENTIVES BUT ADD UP TO A LEVY ON FARMERS BY MARTIAL LAW AUTHORITIES AS MEANS MAINTAIN LOW FOOD PRICES IN POLITICALLY VOLATILE CITIES. CONFIDENTIAL

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8. USAID DIRECTOR HAS TWICE DISCUSSED PROBLEM WITH AFTAB AHMAD KHAN, SECRETARY OF FINANCE AND ECONOMIC AFFAIRS, NOTING BAN ON MOVEMENT CONTRARY TO UNDERSTANDINGS RECENTLY REACHED WITH GOP AND RECORDED IN NEGOTIATING MINUTES OF DECEMBER 1977 PL 480 SALES AGREEMENT. AFTAB APOLOGETIC BUT NOTED HIGHLY UNUSUAL SECURITY PROBLEM WHICH CREATED FORCE MAJEURE SITUATION, AND STATED GOP PROCUREMENT PRICE FOR NEXT CROP WOULD BE RAISED. HE SAID GENERAL ZIA HAD REACTED TO PROPOSED INCREASE IN PRICE OF FLOUR SAYING QTE I DON'T WANT MY BODY DRAGGED THROUGH THE STREETS* UNQTE. AFTAB SAID GOP PLANNED REVIEW WHEAT PRICE AND OTHER INCENTIVES AGAIN SOON WITH VIEW ANNOUNCEMENT OF INCREASE IN

AUGUST/SEPTEMBER WELL BEFORE NEXT PLANTING SEASON.

9. AMBASSADOR IS SENDING LETTER TO SECRETARY-GENERAL

OF FINANCE KAZI EXPRESSING UNDERSTANDING OF DIFFICULT PROBLEMS BUT NOTING CONFLICT WITH DECEMBER 22, 1977 AGREEMENT AND OUR CONCERN FOR EFFECT THESE POLICIES WILL HAVE LONGER-RUN PRODUCTION OUTLOOK. LETTER URGES GOP RECONSIDERATION OF ALTERNATIVES AND EARLY DISCUSSION IN FORM OF TRIMESTER PL 480 MEETING. COPY OF LETTER POUCHED TO DEPARTMENT, AID AND USDA.

10. FROM DEVELOPMENT STANDPOINT WE ARE SERIOUSLY DISTURBED AT THESE DECISIONS AND HAVE SO INFORMED GOP AT APPROPRIATE LEVELS. HOWEVER, WE MUST UNDERSTAND GENUINE SHORT TERM DILEMMA GOP FACES AND EXTENT TO WHICH MARTIAL LAW AUTHORITIES ARE DISCOUNTING THE FUTURE AS THEY STRUGGLE TO GET THROUGH NEXT FEW MONTHS.

11. WE BELIEVE CURRENT SITUATION PROVIDES THE OPPORTUNITY TO START TO DEVELOP AN AGREED MULTI-YEAR PROGRAM WITH THE GOP LINKING REALISTIC AGRICULTURAL
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DEVELOPMENT POLICIES WITH WHAT PAKISTAN CAN EXPECT IN PL 480 ASSISTANCE YEAR-BY-YEAR. DESIRABLE OBJECTIVES OF SUCH A PROGRAM WOULD INCLUDE:

(A) GOP SUPPORT PRICE AND PROCURMENT POLICY WITH EASY ACCESS TO SMALL PRODUCERS AND PRICES COMPATIBLE WITH THOSE IN NEIGHBORING COUNTRIES AS WELL

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AS WITH PAKISTAN'S INPUT COSTS. THIS WOULD MEAN PROCUREMENT PROGRAM EFFORT EQUAL TO SUCCESSFUL EFFORT OF 1976.

(B) ELIMINATION OF MARKETING RESTRICTIONS COMBINED WITH A PROGRAM OF SALES OF GRAIN SUPPLIES FROM RESERVES TO KEEP PRICE WITHIN TOLERABLE LIMITS AND RESTRAIN EXCESSIVE PRICE INCREASES.

(C) PROGRAM OF ACQUIRING AND MAINTAINING A GRAIN RESERVE OF ABOUT A MILLION TONS. IMPORTS WOULD PROVIDE INITIAL INCREMENT AND WOULD REQUIRE ABOUT 500,000 MT OF IMPORTS MORE THAN WERE PREVIOUSLY PLANNED IN PERIOD APRIL 1978 TO APRIL 1979. THIS WOULD MEAN GOVERNMENT WOULD HANDLE OVER 3 MILLION MT THIS YEAR.

(D) REFORM OF THE RATION SYSTEM TO FOCUS IT UPON POOR AND CHECK EXCESSIVE ISSUANCES.

WHILE NOT ALL OF THE ELEMENTS ON THE AMBITIOUS LIST ABOVE CAN BE ACHIEVED IN THE NEXT YEAR OR EVEN A FEW YEARS, WE THINK THE ACTUAL PROGRAM SHOULD BE DEVELOPED COLLEGIAALLY WITH THE GOP, USING THE ABOVE LIST AS A STARTING POINT. WE SHOULD NOT TRY TO HAVE THE GOP COMMIT ITSELF TO MORE THAN IT CAN REALISTICALLY CARRY OUT, BUT WE SHOULD MAKE CLEAR THAT WE WILL EXPECT IT BROADLY TO DO WHAT IT COMMITS ITSELF TO DO AND (IN THE CONTEXT OF CONFIDENTIAL

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A MULTI-YEAR PROGRAM) WHEN IT COMMITS ITSELF TO DO IT. PROGRESS WITHIN AN AGREED TIME FRAME SHOULD BE A GUIDELINE FOR THE AMOUNT OF YEAR-BY-YEAR PL 480 ASSISTANCE THE GOP CAN EXPECT TO RECEIVE: THE BETTER THEIR PERFORMANCE, THE MORE FORTHCOMING WE WOULD BE.

12. AS A START, WE TENTATIVELY SUGGEST A PL 480 PROGRAM LEVEL OF AN ADDITIONAL 150,000 MT OF WHEAT IN FY 78 AND 550,000 MT IN FY 79. THESE AMOUNTS SHOULD HELP PROVIDE THE CUSHION THE GOP WOULD NEED TO TAKE THE DIFFICULT STEPS TO GET AGRICULTURE MOVING AGAIN. SUBSEQUENT YEAR PL 480 PROGRAMS WOULD DEPEND ON THE PROGRAM FORMULATED AND PAKISTANI PERFORMANCE UNDER IT.

13. WE WOULD LIKE TO PURSUE THIS IDEA IN PERIODIC PL 480 MEETINGS AND OTHERWISE AS APPROPRIATE. WE ARE EXPECTING SUCH A REVIEW MEETING WITHIN TWO WEEKS AND WOULD APPRECIATE YOUR COMMENTS AND SUGGESTIONS ASAP. WE ARE CONSIIOUS OF BUDGET CONSTRAINTS AND CURRENT INABILITY TO PROVIDE FIRM COMMITMENTS. BUT WE WOULD APPRECIATE YOUR BEST ESTIMATES OF BALLPARK AMOUNTS AVAILABLE

REMAINDER THIS FY AND IN FY 79.

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